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## WEFA's Projections of Eastern Europe's Trade with the West

WEFA's optimistic view about the prospects for East-West trade over the medium term assumes that the worst of the hard currency credit crunch for Eastern Europe is over.* The following assesses WEFA's projections for Eastern Europe and concludes that several key constraints could prevent the revival in trade portrayed by WEFA. In our view, Eastern Europe will find it difficult to increase its trade with the West to any significant degree over the next few years, and indeed will be doing well to maintain the average levels of the late 1970s. 25X1

### WEFA Views of Eastern Europe's Financial Situation

WEFA does not take into account that, despite recent improvements in East European foreign trade performance, Western commercial banks believe that they are "loaned up" to most East European countries (Czechoslovakia and Bulgaria are two possible exceptions), or that the financial problems currently facing Yugoslavia are hurting other countries in the area. Most of the East European countries have made important adjustments in their foreign trade balances, but so far these changes have been largely focused on severe import cuts rather than strong export expansion efforts. East Germany apparently has tried to do both. Such sharp import reductions damage prospects for economic recovery and export growth. 25X1

Although WEFA correctly states that the current financial crises in three Latin American countries have put East European hard currency indebtedness into "a new perspective," it fails to point out that Western bankers are still refusing to provide new money to Eastern Europe and continue to regard the area as a poor credit risk. In the eyes of Western bankers, the East European return to creditworthiness is at best likely to be a slow process. On the other hand, WEFA does not consider that West European governments, in support of their own domestic economic recovery efforts, may ease the resulting trade financing gap by providing more liberal export credit and guarantee programs for West European export sales to Eastern Europe. If this happens, the East European financial picture could brighten. 25X1

WEFA puts a great deal of stock in the "savings" that the East European countries could realize from declining world interest rates. It does not take into account that the fundamental economic and fiscal conservatism of many of the East European regimes might instead dictate that these "savings" be used to reduce the outstanding hard currency debt and to rebuild seriously depleted reserves. Instead, this reaction is

* WEFA, December 23, 1982 and commented on in the *Financial Times*, January 24, 1983. 25X1

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explicitly discounted as being unlikely on economic policy grounds, without adequate clarification. WEFA may now be altering its optimistic outlook since, in a more recent publication,* it presents a pessimistic assessment of the East European debt situation. In any case, linkage between the debt and the trade outlook is inescapable. 25X1

## Outlook for Imports

WEFA's assertion that East European imports from the West will grow an average of 15 percent annually in nominal terms during the next five years neglects several factors. These include the burden of the East Europeans' large debt servicing obligations, and the extent to which these countries have had to draw down the level of their hard currency reserves, and to use hard currency commitments previously extended by Western banks to make loan payments due in recent months. 25X1

WEFA also forecasts a continuing reduction in East European hard currency grain imports after cuts of these imports by an estimated 50-70 percent in marketing year 1981-1982. WEFA does not consider the internal political difficulties that the East European regimes might be faced with if meat supplies decline because of these import cutbacks. Rising meat consumption has long been a point of economic and political pride for East European regimes and is not something they would want to risk lightly. 25X1

## Prospects for East European Exports

WEFA expects East European exports to the developed West to revive and grow by 8.5 percent in nominal terms in 1983, after dropping about $2.4 billion (by over 12 percent) from 1980 to 1982. Moreover, WEFA's export projections assume that Eastern Europe will be able to gain a larger share of Western markets in the next five years, by boosting real exports an average of 4.5 percent per annum. WEFA overestimates the ability of the East European economies to increase the pace and the quantity of their production for export, and does not suggest how these increases are to be achieved. Even if WEFA's projection, for OECD growth holds true, lagging productivity, poor quality controls, and potential competition from Third World countries will keep Eastern Europe from capturing a larger share of this market. 25X1

WEFA also assumes that the Polish economy will recover in 1983. Poland, in fact, cannot presently afford to import the hard goods from the West that it needs for economic revival, and its export prospects--even for coal--are bleak. 25X1

* WEFA, January 25, 1983

Other Determinants of Trends in East-West Trade

WEFA also neglects to address several other factors that will influence the growth of East European trade with the developed West, such as:

-- the questionable capacity of East European economies to absorb Western technology effectively;

-- the ricochet effects of cutbacks in East European investment in capital equipment and plant modernization on the future competitiveness of East European goods in Western and even Third World markets;

-- the impact that a sharp drop, or even steady decline, in world energy prices would have on East European oil product exports such as gasoline, petrochemicals, and plastics. This, in turn, could cause a reduction in hard currency earnings, particularly for Bulgaria and East Germany; and

-- the continuing impact of the cool East-West political climate on trade prospects with Eastern Europe. 25X1

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US Treasury